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TPE&C

1981 Executive Compensation Study

500 Largest Industrials

The Top and Bottom

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TPF&C Executive Compensation Study

TPF&C's annual study of executive compensation focuses on the design, amounts and growth rates of the compensation packages received by senior executives of major U.S. industrials. Through most of the 1970s, we highlighted the Top 100 U.S. industrials*; in 1980, we expanded our survey to include the Bottom 100*, the last 100 of the Top 500 industrials.

Last year was a landmark in executive compensation. For the first time, a chief executive in a Top 100 company earned total cash compensation (salary plus annual bonus) of more than $1,000,000. In fact, five chief executives broke the million dollar barrier.

Total cash compensation statistics, financial characteristics of the survey companies and demographics of the chief executive officers make up the first section of the report. The second section explores the extent to which the incentive pay practices of the Bottom 100 mirror those of the Top 100. As in earlier studies, the report contains a company-by-company listing of the short- and long-term incentive compensation techniques included in the current plans of the Top 100 organizations.

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*almost identical to the *Fortune* listings (May 1981), exceptions noted on pages 13 and 16.

Profile of the Survey Group

The Companies

For the second year in a row, Exxon, with sales of $103 billion, was the first of the Top 100 companies. Median sales for the group were $6.1 billion. In contrast, median annual sales for the Bottom 100 were $540 million.

In both groups, sales grew more slowly in 1980 than they did in the previous year. Median sales increases were 11.7% higher than 1979 in the Top 100 and 10.2% higher in the Bottom 100, as shown in *Exhibit 1*. (The comparable 1978-1979 statistics were 18.2% and 16.4%.) Although the median increase in profits was 12.2% in the Top 100, the Bottom 100 registered only a 2.7% increase over 1979. These rates were also significantly less than the 1978-1979 results of 25.1% and 17.5% for the Top 100 and Bottom 100 respectively.

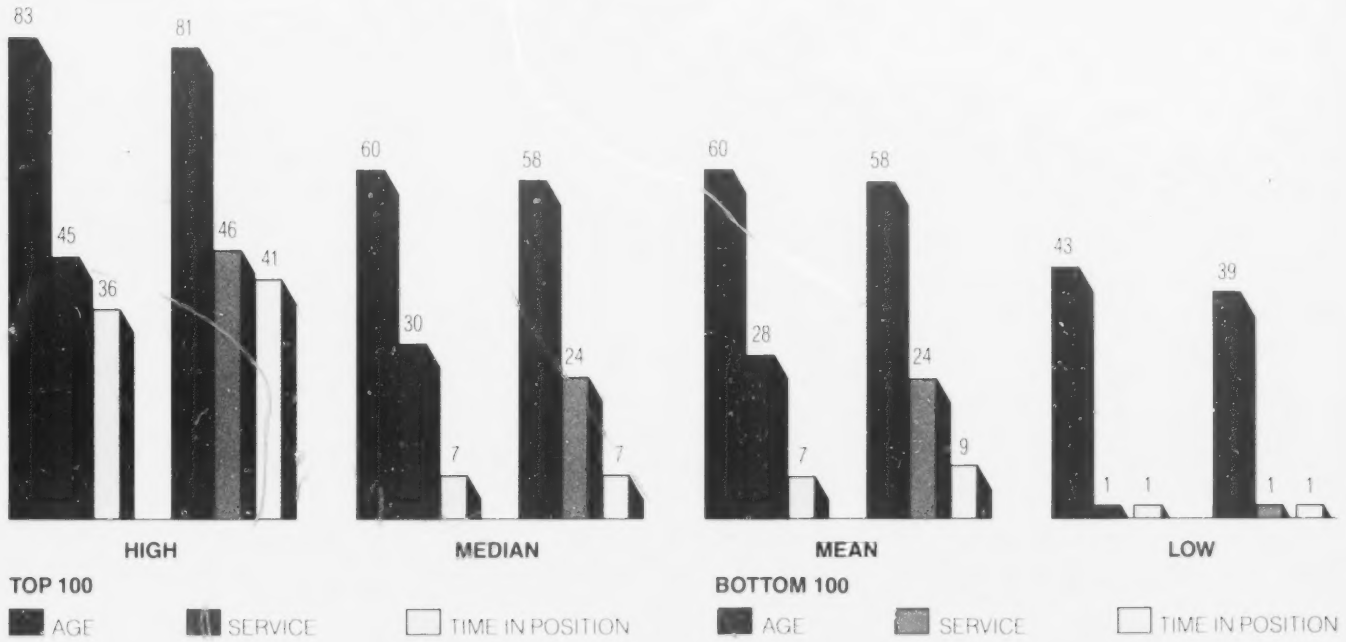
The CEOs

As we noted, five CEOs received 1980 annual cash compensation exceeding $1,000,000. All five also were eligible to receive gains from unexercised stock options and four of them were eligible to receive compensation from long-term performance incentive plans.

The average CEO in a Top 100 company was 60 years old, had been in the position for seven years and had company service of approximately 28 years *(Exhibit 2)*. A Bottom 100 CEO tended to be slightly younger, with an average age of 58, had held the position a bit longer, for an average of nine years, and had 24 years of service with the company.

EXHIBIT 1
Financial Statistics

EXHIBIT 2
Personal Statistics



Total Compensation

Exhibit 3 shows the range and the mean and median values of the total cash compensation reported for the five highest paid executives in both the Top 100 and Bottom 100 groups. Although it is generally accepted that pay levels and company size are positively correlated, factors other than sales also account for variation in pay.

EXHIBIT 3

1980 Total Cash Compensation Statistics

*CEO is not always the highest paid

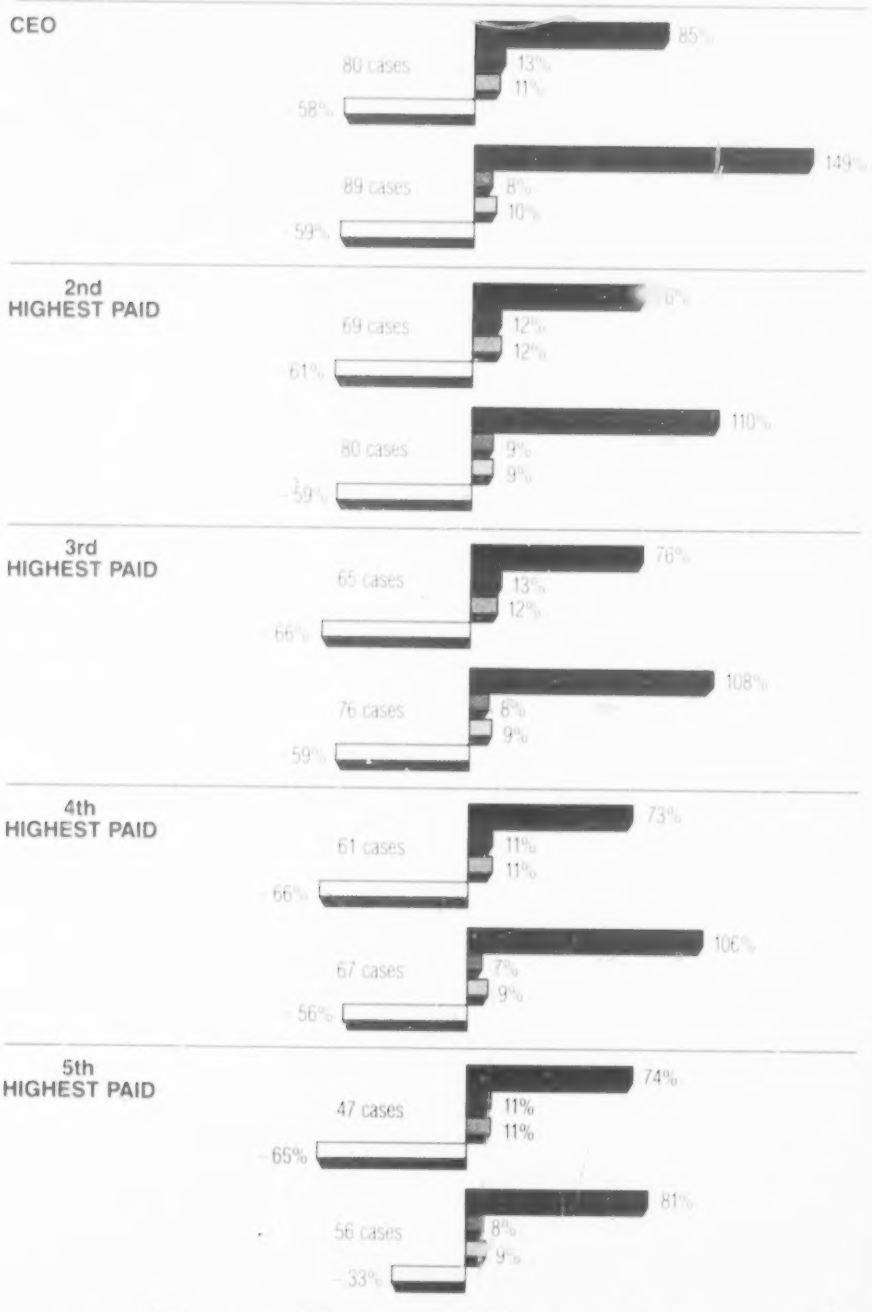
Increases in Compensation

Median increases in total cash compensation for 1980 were lower for the five highest paid executives in the Bottom 100 companies than they were in the Top 100, as shown in *Exhibit 4*. The profit performance of the Bottom 100 may have negatively affected executive pay increases.

The combined median increase for the five highest paid executives in the Top 100 was slightly above the 1980 increase of 12.4% in the Consumer Price Index. Bottom 100 company executives' pay did not even keep pace with the CPI increase.

EXHIBIT 4

Percentage Increase in Total Cash Compensation – 1979-1980*



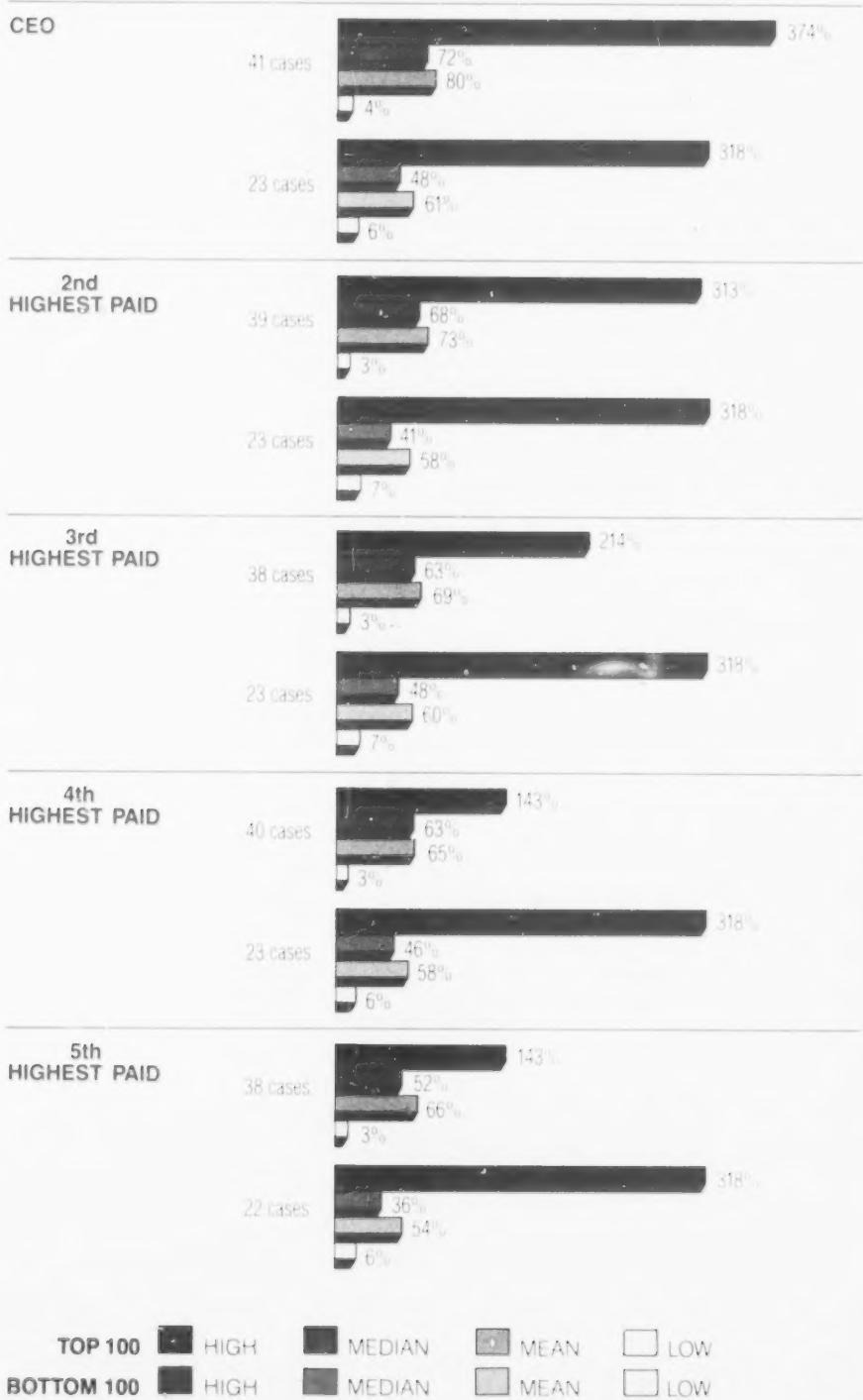
*These increases were determined for those executives who occupied the same position in both 1979 and 1980.

Salary/Bonus Mix

As was the case in our last study, only about 25% of the 200 companies reported salary and bonus figures separately. Therefore, the results shown in *Exhibit 5* may not be representative of the entire survey group. In all five executive positions in the Top 100, bonus as a percent of base salary was higher than that of comparable positions in the Bottom 100.

EXHIBIT 5

Bonus as a Percent of Base Salary



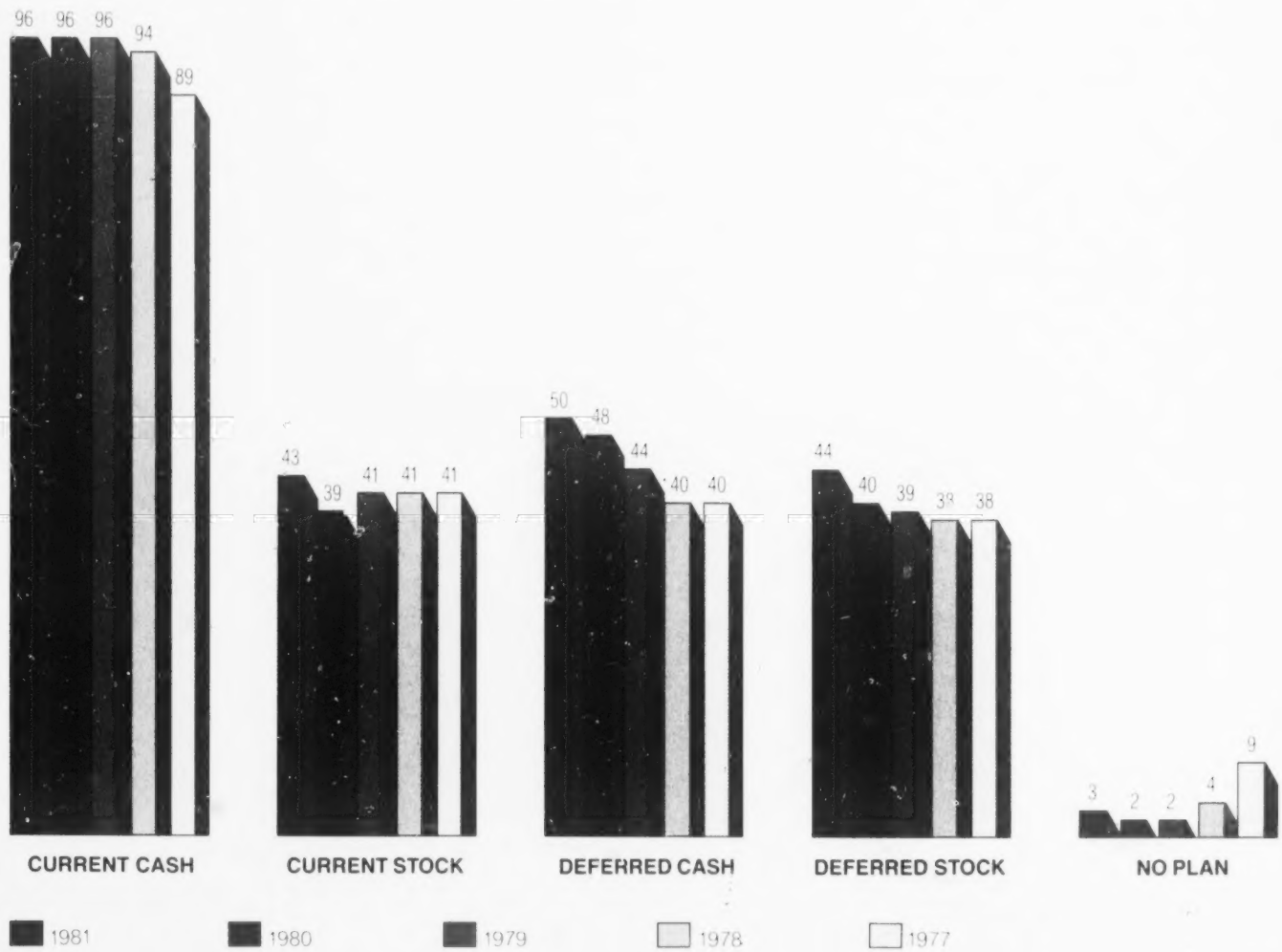
Incentive Compensation Techniques

Either short-term or long-term incentive compensation plans are incorporated in the executive compensation programs of all but two companies in the study. In fact, 92 of the Top 100 companies provide for both short- and long-term incentives for their executives. Among the Bottom 100 companies, 76 provide both forms of incentive compensation.

Exhibits 6 and *8* review the short- and long-term incentive pay practices of the Top 100 companies during the past five years. *Exhibits 7* and *9* contrast the current practices of the Top 100 and Bottom 100 companies. The company-by-company listings in *Exhibit 10* indicate the types of awards that each of the Top 100 companies may use under the terms of its plans as reported to shareholders.

EXHIBIT 6

Summary of Top 100 Short-Term Incentive Trends – 1977-1981



Short-Term Incentives

There is little room for expansion of annual bonus plans among the Top 100 industrials, as they are now reported by 97 companies. In contrast, 87 of the Bottom 100 companies report annual bonus plans.

Paying awards in cash as soon as practical after the close of the fiscal year continues to be the most popular form of payment. The forms of payment are defined below.

Exhibit 7 shows the extent to which the various forms of payment are provided for among those companies that sponsor annual bonus plans. The Bottom 100 companies show an even stronger tendency for current cash awards than do the Top 100, and they are considerably less interested in deferred awards or awards paid in stock.

Definitions

To ensure consistent interpretation of study results, we define the various short-term awards as follows:

- *Current Cash*

  Any award paid in cash either immediately following the close of the year on which the award is based or in installments beginning in that year and continuing for a number of years during active employment.

- *Current Stock*

  Any award paid in stock either immediately following the close of the year on which the award is based or in installments beginning in that year and continuing for a number of years during active employment.

- *Deferred Cash*

  Any award paid in cash, but not until termination or retirement. The fact that the payment at termination or retirement might be in a lump sum or spread over several annual installments is not considered in this study and does not affect this classification. Similarly, there is no analysis of any increase (e.g., interest payments) in the award amount during the deferral period.

- *Deferred Stock*

  Any award made in stock under the short-term incentive plan, but not paid until termination or retirement. The fact that the payment at termination or retirement might be in a lump sum or spread over several annual installments is not considered in this study and does not affect this classification. Similarly, there is no analysis of any increase (e.g., market price gains and/or dividend equivalents) in the award amount during the deferral period.

EXHIBIT 7

Comparison of Short-Term Forms of Payment*

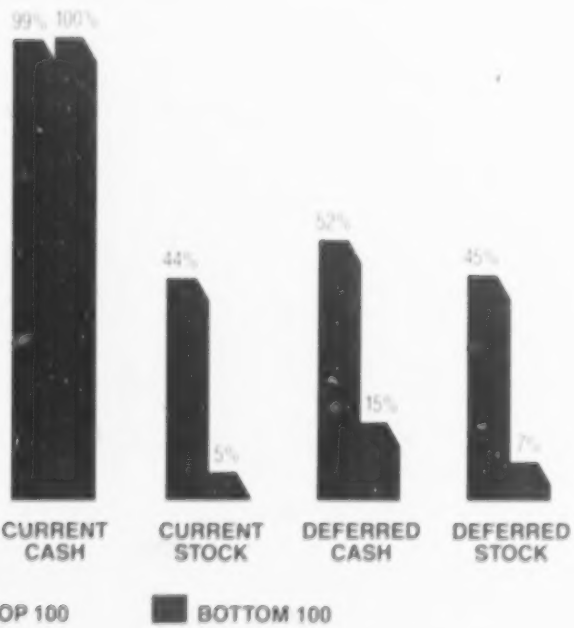


*Figure indicates the extent to which the form of payment is provided for among those companies that offer short-term plans.

Long-Term Incentives

Are U.S. companies too concerned with short-term profitability? Not if the prevalence of long-term executive compensation programs is any indication. Of the Top 100, 95 use some form of long-term executive compensation. Stock options, employed by 87 companies, remain the most prevalent long-term device. In 73 of these companies, stock appreciation rights may be attached to the option. *Exhibit 8* traces Top 100 trends in long-term incentive compensation over the past five years. The steady increase in performance-based (share or unit) programs continued in 1980. Similar trends were observed in the Bottom 100. Although only 78 of the Bottom 100 reported stock option plans, 87 companies reported some form of long-term executive compensation device in 1980, up from 83 in 1979.

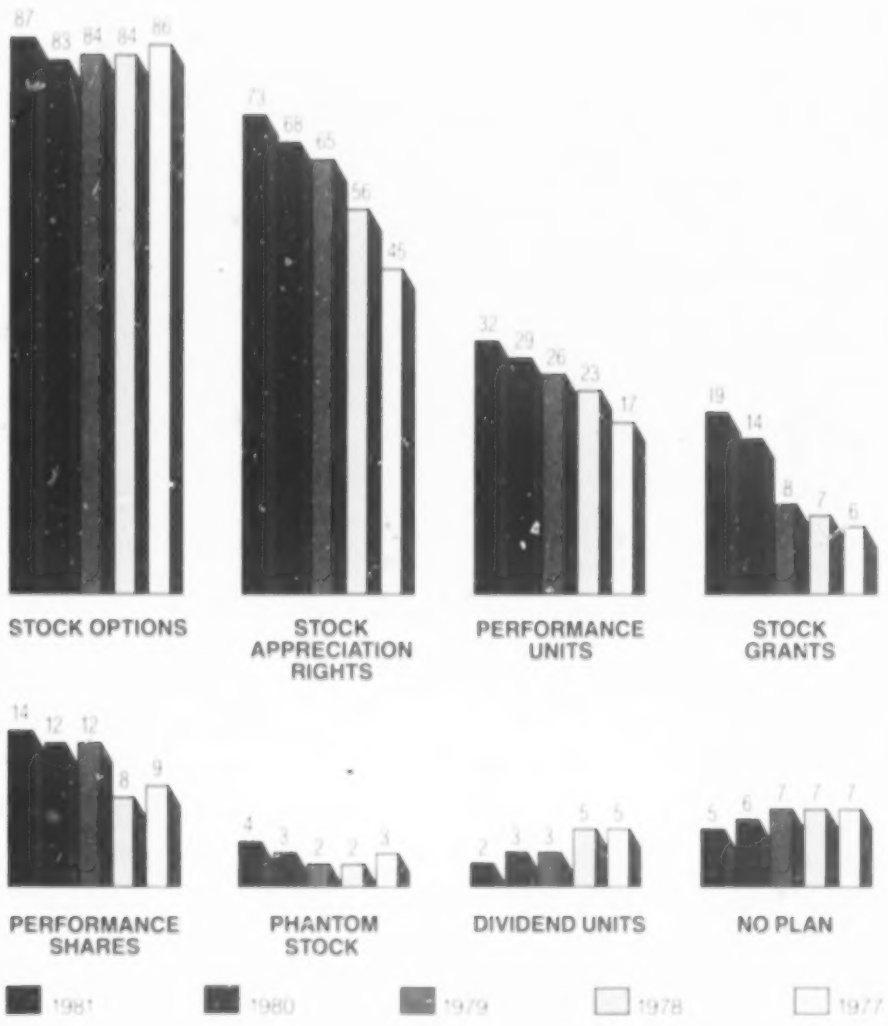
Long-term incentive compensation may be a critical issue in very large companies in 1982. Historically, these plans have been justified on the basis of providing the executive with a powerful economic inducement to make decisions that enhance long-term profitability. But even though the overwhelming majority of U.S. companies employ long-term incentive programs in their executive compensation packages, American industry continues to be criticized for an excessive short-term focus – if anything, the criticism has intensified.

This raises many questions. If incentive awards do in fact support long-term strategic goals, should compensation plans be redesigned to focus more heavily on all long-term financial and nonfinancial goals? Should the potential payout from performance-based plans be increased to "tilt the balance" of the executive package toward the long-term opportunity? Or, will the impetus be in the other direction, with a resurgence of stock options as a result of the favorable tax treatment provided under the Economic Recovery Tax Act of 1981? The future, as always, is difficult to predict. There is no doubt, however, that, over the next several years, companies will be scrutinizing their long-term plans quite closely, and that over the next year some significant shifts will have occurred in the relative prevalence of the various incentive devices within our Top 100 and Bottom 100 survey groups.

Definitions of the various long-term executive incentive devices follow *Exhibit 8*.

EXHIBIT 8

Summary of Top 100 Long-Term Incentive Trends – 1977-1981



Definitions

We define the various long-term awards as follows:

- *Stock Options*

  An opportunity to purchase company stock in the future at a predetermined price.

- *Stock Appreciation Rights*

  A right granted in connection with an option where the executive, in lieu of exercising the option, can receive a payment equal to the amount by which the fair market value of the stock, on the date the option otherwise would have been exercised, exceeds the option price. These payments can be made in cash or free shares of stock having an equivalent value, or a combination of both.

- *Performance Unit Awards*

  Any grant of contingent units that are "earned out" by meeting preestablished performance goals over a predetermined span of time (usually three to six years). Such units, when earned, are assigned an arbitrary value that is not related to the *then* current market price of the company's stock. Payment is made in cash or equivalent shares of stock.

- *Performance Share Awards*

  Any grant of contingent units that are "earned out" by meeting preestablished performance goals over a predetermined span of time (usually three to six years). When earned, each of the units awarded to an employee is converted to a share of common stock. Alternatively, the employee may receive the cash equivalent of the common stock or a combination of cash and stock. Performance goals are most often stated in terms of earnings-per-share growth, but other measures may be used.

- *Stock Grants*

  Grants of stock or stock units at no or nominal cost. In some instances, the stock is nontransferable and/or subject to substantial risk of forfeiture until some special conditions are met. This is called restricted stock. The restrictions are typically designed to lapse over a period of years, based on continuing service or achievement of predetermined financial objectives.

- *Phantom Stock*

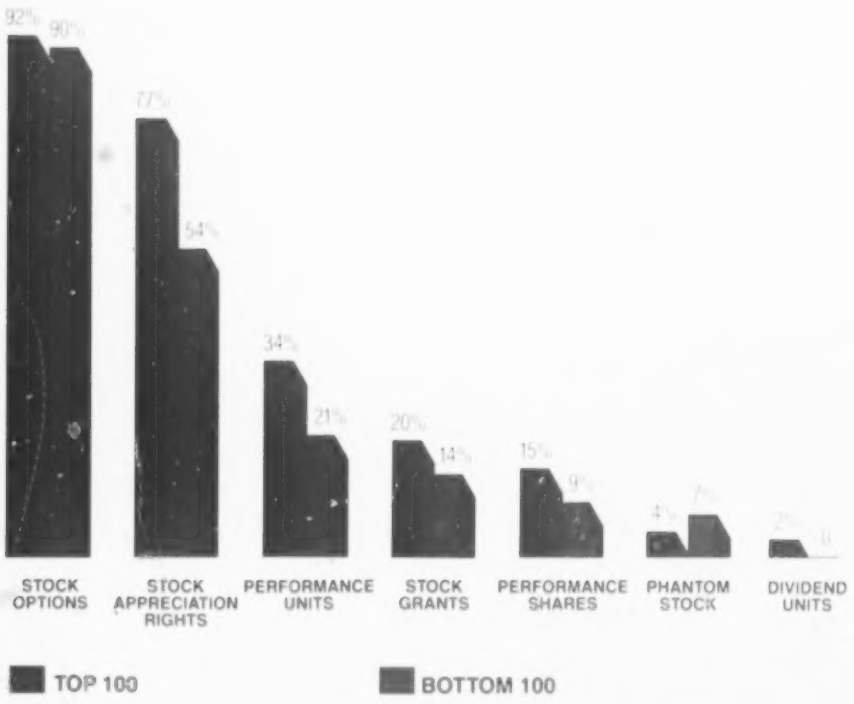
  Any award made in units analogous to an actual share of stock where the employee receives, after a period of time, the equivalent of the appreciation in the value of the underlying stock. This sum may be paid out either in cash or in stock.

- *Dividend Units*

  Any award made in units analogous to an actual share of stock where the employee receives only the equivalent of dividends paid on shares of the company's stock. This sum may be paid out either in cash or in stock over a stated number of years.

EXHIBIT 9

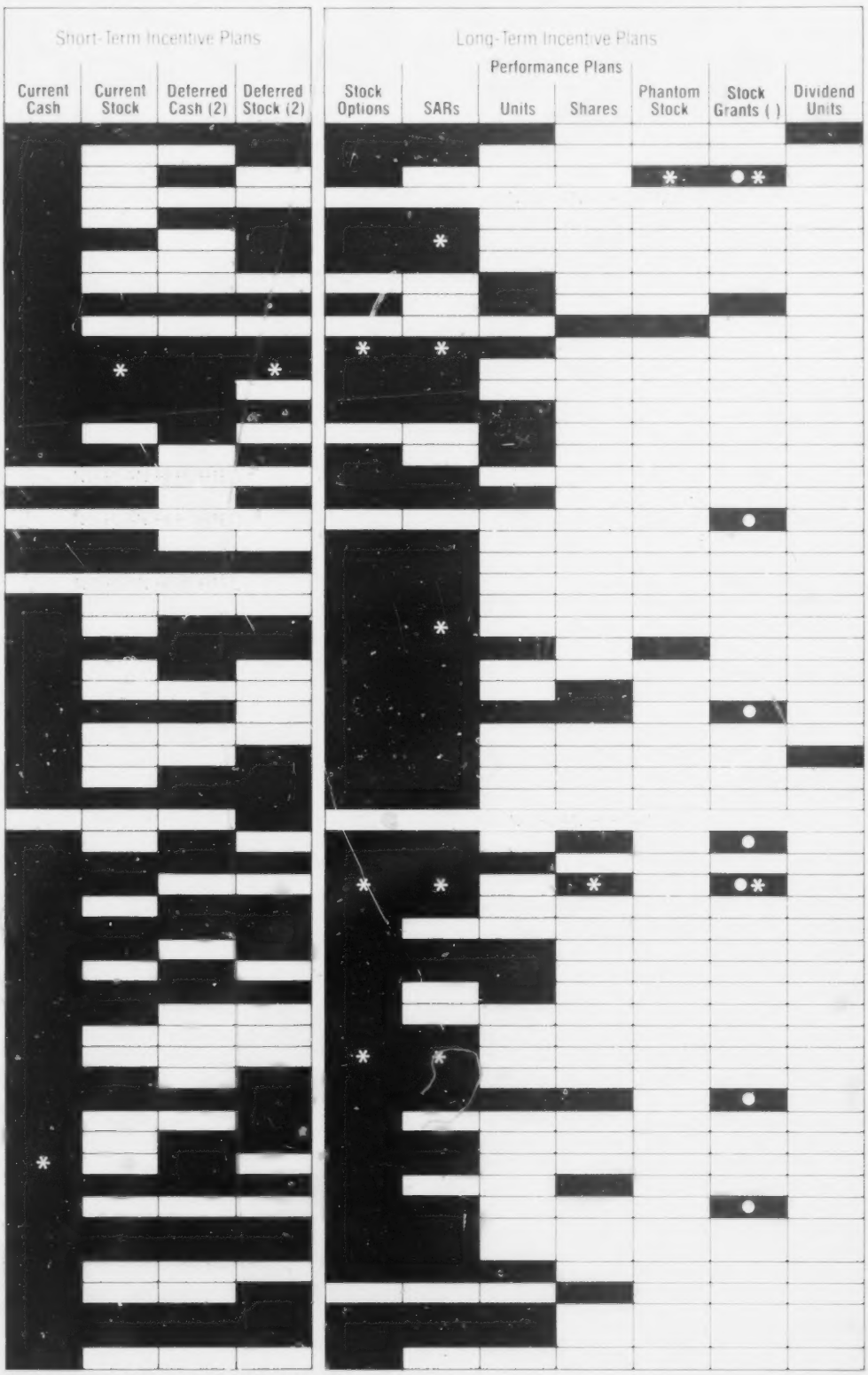
Comparison of Long-Term Incentive Techniques*



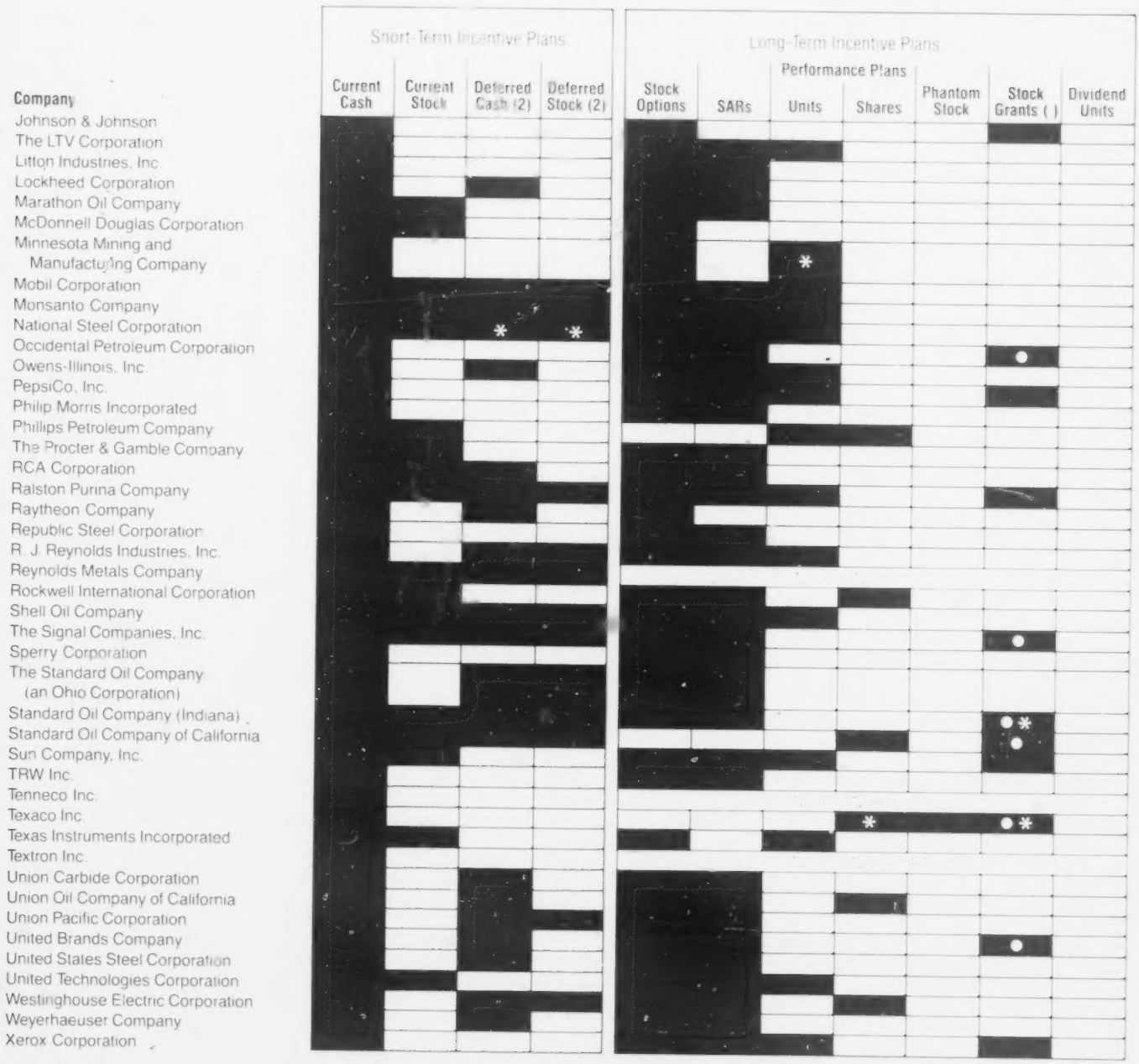
*Data indicate the percentage of companies in each group that use the technique.

EXHIBIT 10

Short- and Long-Term Incentive Plans in the Top 100 U.S. Industrial Companies (1)



Darker color indicates feature included in plan



(1) Companies are those ranked by *Fortune* (May 1981). Reynolds Metals Company and Textron Inc. have been substituted for Farmland Industries, Inc. and Western Electric.

(2) Deferred awards indicate payout after termination or retirement and do not include individual contractual deferred compensation arrangements.

(●) Restricted stock.

(✱) New feature adopted in 1981.

Please note that this chart reports methods of payment for which the companies have made provisions in their plans, but does not necessarily indicate methods of payment actually used.

Summary and Conclusions

This year's review of executive compensation practices and trends reveals that, despite slower growth rates in corporate sales and profits, total cash compensation for senior executives in the Top 100 companies continues to increase at a steady 10% to 13% rate. The rate of pay increase for senior executives in the Bottom 100, however, has declined – at least temporarily. Median increases in total cash compensation in 1980 were down several percentage points from 1979. The long-term incentive compensation trend continued, with more companies than ever before reporting plans. Although stock options remain the most prevalent long-term executive incentive, the trend toward non-market-price based "performance plans" continued. In level of compensation, rate of increases and prevalence of plans, the Bottom 100 trails the Top 100 but reflects the same trends.

Looking ahead, the major factors influencing the design of executive compensation programs will be:

- the Economic Recovery Tax Act
- increasing concern over the reasonableness of executive compensation levels and the performance criteria for earning incentive awards (both short- and long-term).

One immediate result of the new tax law will be the restoration of interest in stock options. With no tax liability at exercise, a reduced capital gains tax on appreciation and lower capital gains rates, executives may find stock options as alluring as they were in pre-1970 days. Over the past decade, many companies have moved away from market-price based incentives, reasoning that if executives are to be rewarded for long-term business results, the rewards should be based on measures (such as earnings-per-share growth) that the executives can influence and that will truly mirror their performance. The stock market's unpredictable behavior does not necessarily produce a close linkage between executive performance and bonus awards; therefore, the performance share/performance unit generation of incentives came into being.

Do long-term performance plans that pay off on, say, earnings-per-share growth really influence whether earnings per share increase or do they, as skeptics claim, simply cost a company more in compensation when targets established years in advance are exceeded? Do these plans actually encourage executives to make the hard decisions that might depress profits one year but boost them over the next two or three? Or are U.S. executives excessively motivated toward short-term profitability, notwithstanding the presence of a plan that rewards long-term performance? If executive orientation is still too short term, perhaps long-term performance targets, and the underlying rewards, should be tied more closely to the corporation's long-term strategic goals. We could then expect to see a continuing de-emphasis on all market-based incentives, and an increased emphasis on performance-based, long-term plans.

Yet an equally tempting strategy is now available to compensation planners. They could assume that performance-based plans have not demonstrably changed the executive's short-term profit orientation and use the tax-effectiveness of stock options as a reason for returning to a program consisting solely of market-based incentives. The new incentive stock option, created by the 1981 tax act, is particularly appealing to the executive because of its treatment of capital gains. What better way to link executive and shareholder interests than through stock options? Do shareholders care how an executive implements a long-term strategy or how fast earnings grow? If the market price goes up, the shareholders should be willing to pay executives handsomely, regardless of how much executive performance influenced the market value. Should this latter strategy prevail, future tabulations of Top 100 practices probably will show a reversal of the recent performance plan trend and a return to stock options as the principal, if not the exclusive, source of long-term executive compensation.

Will incentive compensation actually come full circle and return to the practices of the 1960s when favorable tax treatment (accompanied by some healthy market action) made options attractive? Probably not. Executives will not want all their long-term rewards riding on an unpredictable market. And many companies will still view performance-based plans favorably because they can be closely tied to strategic business plans and they can reward divisional as well as corporate performance (a significant advantage in today's world of diversified businesses). The full impact of any changes probably will not be reflected in the practices of the Top 100 for several years. But given the importance of the executive compensation issues now facing major U.S. companies, the design and form of compensation will doubtless continue to command high priority among executives and Board compensation committees.

EXHIBIT 11

Alphabetical Listing of Bottom 100* Companies

American Bakeries Company
American Hoist & Derrick Company
Avery International Corporation
Bally Manufacturing Corporation
Bausch & Lomb Incorporated
Beckman Instruments, Inc.
Bell & Howell Company
Bemis Company, Inc.
Big Three Industries, Inc.
Bucyrus-Erie Company
Bunker Ramo Corporation
CBI Industries, Inc.
Cameron Iron Works, Inc.
Cannon Mills Company
Capital Cities Communications, Inc.
Carpenter Technology Corporation
Chicago Pneumatic Tool Company
The Clorox Company
Collins & Aikman Corporation
Columbia Pictures Industries, Inc.
Consolidated Papers, Inc.
Copperweld Corporation
DPF Incorporated
Dan River Inc.
Data General Corporation
Dean Foods Company
Dennison Manufacturing Company
The Dexter Corporation
Dorchester Gas Corporation
The Dorsey Corporation
Dow Jones & Company, Inc.
EG&G, Inc.
Eagle-Picher Industries, Inc.
Economics Laboratory, Inc.
Envirotech Corporation
Federal Paper Board Company, Inc.
Ferro Corporation
Fieldcrest Mills, Inc.
Fleetwood Enterprises, Inc.
The Foxboro Company
Frederick & Herrud, Inc.
General Refractories Company
Gerber Products Company
Gifford-Hill & Company, Inc.
Gulf Resources & Chemical Corporation
Harcourt Brace Jovanovich, Inc.
Harnischfeger Corporation
Hart Schaffner & Marx
Hoover Universal, Inc.
Hyster Company
Ideal Basic Industries, Inc.
Idle Wild Foods, Inc.
Insilco Corporation
International Flavors & Fragrances Inc.
Kane-Miller Corp.
Kellwood Company
M. Lowenstein Corporation
Macmillan, Inc.
Magic Chef, Inc.
Maryland Cup Corporation
Masonite Corporation
McCormick & Company, Incorporated
McLouth Steel Corporation
Metromedia, Inc.
Mitchell Energy & Development Corp.
Moore McCormack Resources, Inc.
Nalco Chemical Company
Nashua Corporation
Norris Industries, Inc.
Nucor Corporation
Outboard Marine Corporation
Peabody International Corporation
H. K. Porter Company, Inc.
Purex Industries, Inc.
Questor Corporation
Raychem Corporation
H. H. Robertson Company
Rohr Industries, Inc.
Savannah Foods & Industries, Inc.
The Scott & Fetzer Company
Sheller-Globe Corporation
Signode Corporation
A. O. Smith Corporation
Sonoco Products Company
Stokely-Van Camp, Inc.
Storage Technology Corporation
Sun Chemical Corporation
Thiokol Corporation
Todd Shipyards Corporation
Trinity Industries, Inc.
Tyler Corporation
United Merchants and Manufacturers, Inc.
VF Corporation
Varian Associates, Inc.
Wang Laboratories, Inc.
Warnaco Inc.
The Washington Post Company
Westmoreland Coal Company
Wm. Wrigley Jr. Company
Wyman-Gordon Company

*Companies are those ranked 401-500 by *Fortune* (May 1981). Some of these companies have recently merged or are not required to file proxy statements with the SEC. Consequently, Bally Manufacturing Corporation, Bemis Company, Inc., CBI Industries, Inc., Cameron Iron Works, Inc., Columbia Pictures Industries, Inc., Ferro Corporation, Hart Schaffner & Marx, Hyster Company, Outboard Marine Corporation, Peabody International Corporation, Purex Industries, Inc., Signode Corporation, A. O. Smith Corporation and Thiokol Corporation have been substituted for Ampex Corporation, The Coca-Cola Bottling Company of New York, Inc., Fairmont Foods Company, Fiat-Allis Construction Machinery, Inc., Freeport Minerals Company, Hobart Corporation, H. P. Hood Inc., The Marley Company, McDonough Co., Midland Cooperatives, Inc., National Cooperative Refinery Association, National Starch & Chemical Corporation, United Refining Company and Wallace-Murray Corporation.

About TPF&C

We have been consultants to management since 1917. TPF&C currently employs more than 1500 persons and has a consulting and specialized support staff of over 1000.

We serve more than 4000 clients in the private and public sectors, about 500 of whom are multinational organizations. Our clients have operations in over 90 countries.

As consultants to management, we relate our services to a number of important business problems. Our clients typically recognize the value of outside counsel in light of today's demands on management for ready access to the diversity of skills and knowledge required to keep pace with rapidly changing technologies, markets and cultures.

We have 28 consulting offices worldwide – 17 in the U.S., four in Canada, four in Europe, two in Latin America and one in the Far East – to better serve our growing list of clients.

Our consulting skills are in these fields:

- executive compensation
- salary administration
- marketing and sales compensation
- actuarial and employee benefits
- communications
- human resource management
- management, organization and planning
- health care management/HMOs
- risk management
- insurance company actuarial and management services

TPF&C Compensation Data Bank and Compensation Determination Service

TPF&C's Compensation Data Bank provides annual surveys for participating companies, evaluating base salary, total cash compensation and base salary midpoints. CDB also sponsors a special biennial survey of long-term incentive plans that permits comparison of different types of award.

The Compensation Determination Service provides analysis of pay policies and practices, and uses composite mathematical models to identify factors in pay differentials that cannot be attributed to variances in job content.

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